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Executive Director



*Public Utility Commission of Texas*

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FCC MAIL ROOM

Magalie Roman Salas  
Office of the Secretary  
Federal Communications Commission  
445 12<sup>th</sup> Street, S.W.  
Washington, D.C. 20554

RE: CC Docket No. 96-98/99-68 (FCC 00-227)  
Inter-Carrier Compensation for ISP-Bound Traffic

To the Secretary:

Enclosed herewith for filing with the Commission are an original plus four copies of the Comments of the Public Utility Commission of Texas in the above captioned matter. We are providing copies to ITS and the Competitive Pricing Division. We are also providing an electronic copy of these comments via your ECFS interface.

Sincerely,

*Stephen J. Davis*

Stephen J. Davis  
Director, Office of Policy Development

cc: ITS, Inc.  
Chief, Competitive Pricing Division

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Before the  
Federal Communications Commission  
Washington, D.C. 20554

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In the Matter of	)	
	)	
Implementation of the Local Competition	)	CC Docket No. 96-98
Provisions in the Telecommunications Act	)	
of 1996	)	
	)	
Inter-Carrier Compensation	)	CC Docket No. 99-68
for ISP-Bound Traffic	)	(FCC 00-227)

COMMENTS OF THE  
PUBLIC UTILITY COMMISSION OF TEXAS

In a Public Notice released June 23, 2000,<sup>1</sup> the Federal Communications Commission ("FCC" or "Commission") seeks comment on a number of issues related to the remand of its *Reciprocal Compensation Ruling*<sup>2</sup> by the United States Court of Appeals for the D.C. Circuit.<sup>3</sup> The Public Utility Commission of Texas (PUCT), having jurisdiction over telecommunications services in Texas, herein provides its comments in response to the Public Notice. The PUCT provided Comments in April 1999 on the FCC's initial NPRM in this proceeding.<sup>4</sup>

The Court of Appeals vacated the FCC's *Reciprocal Compensation Ruling* and remanded the proceeding for want of reasoned decision-making. The appellate court concluded that the FCC did not justify its end-to-end analysis in terms of the statute or the FCC's own regulations in determining whether a call to an ISP is subject to the reciprocal compensation

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<sup>1</sup> *Public Notice: Comment Sought on Remand of the Commission's Reciprocal Compensation Declaratory Ruling by the U.S. Court of Appeals for the D.C. Circuit, CC Docket Nos. 96-98, 99-68, FCC 00-227 (June 23, 1999).*

<sup>2</sup> *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Inter-Carrier Compensation for ISP-Bound Traffic, Declaratory Ruling in CC Docket No. 96-98 and Notice of Proposed Rulemaking in CC Docket No. 99-68, FCC 99-38, 14 FCC Rcd 3689 (1999) (Reciprocal Compensation Ruling).*

<sup>3</sup> *Bell Atl. Tel. Companies v. F.C.C.*, 206 F.3d 1 (D.C. Cir. 2000).

<sup>4</sup> *Comments of the Public Utility Commission of Texas, CC Docket Nos. 96-98 and 99-68 (Apr 8, 1999).*

requirement of section 251(b)(5). The FCC now seeks further comment on the issues identified by the court in its decision: the jurisdictional nature of ISP-bound traffic, the scope of the reciprocal compensation requirement of section 251(b)(5), and the relevance of the concepts of “termination,” “telephone exchange service,” “exchange access service,” and “information access.” The Commission also seeks comment regarding any new or innovative inter-carrier compensation arrangements for ISP-bound traffic that parties may be considering or may have entered into, either voluntarily or at the direction of a state commission.

In these Comments, the PUCT will support its position that ISP-bound traffic should be considered local for the purpose of applying reciprocal compensation rates, and we will argue that section 251(b)(5) does not preempt state authority. We are providing a copy of a new decision by the PUCT in a proceeding involving reciprocal compensation, and we offer one recommendation for a reexamination of FCC rules.

### **The Jurisdictional Nature of ISP-Bound Traffic**

The PUCT considers ISP-bound traffic to be local for the purpose of applying reciprocal compensation rates. We disagree with the Commission’s conclusion in the *Reciprocal Compensation Ruling*, based an end-to-end analysis, that ISP-bound calls are not local calls. The history of our evidentiary proceedings, and the appeals of those rulings, supports our view.

The PUCT initially addressed the issue of reciprocal compensation in late 1996 in the First Mega-Arbitration Award,<sup>5</sup> establishing a “bill and keep” mechanism for such

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<sup>5</sup> *Petition of MFS Communications Company, Inc. for Arbitration of Pricing of Unbundled Loops*

compensation. In 1997, the PUCT issued the Second Mega-Arbitration Award<sup>6</sup> in which permanent inter-carrier compensation rates were established. The scope of the reciprocal compensation provisions approved in the Mega-Arbitration proceedings was disputed in a subsequent proceeding<sup>7</sup> that specifically involved ISP-bound traffic. Despite Southwestern Bell Telephone Company (“SWBT”) arguments that ISP-bound traffic should be considered jurisdictionally interstate, the PUCT determined that such traffic is local, and should be subject to reciprocal compensation for the transport and termination of local traffic. The PUCT concluded that calls over the Internet consist of two components: the information component, which is the content of the call, and the network component, which is the carrier-to-carrier and carrier-to-end-user telecommunications transmission of the call. SWBT appealed the PUCT decision to federal district court, where the court upheld the PUCT decision,<sup>8</sup> agreeing that, under the interconnection agreements, “local traffic” includes calls to ISPs. Specifically, the district court agreed with the notion that a “call” from a SWBT customer to a Time Warner ISP customer terminates locally at the ISP’s facility. SWBT then appealed the PUCT and district court decisions to the U.S. Court of Appeals for the Fifth Circuit.<sup>9</sup> The Court of Appeals held that the PUC and the district court had jurisdiction to adjudicate the merits of this case and

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*Agreement Between MFS Communications Company, Inc. and Southwestern Bell Telephone Company*, Docket No. 16189, *et al*, Award (Nov. 8, 1996) (First Mega-Arbitration Award).

<sup>6</sup> *Petition of MFS Communications Company, Inc. for Arbitration of Pricing of Unbundled Loops Agreement Between MFS Communications Company, Inc. and Southwestern Bell Telephone Company*, Docket No. 16189, *et al*, Award (Dec. 19, 1997) (Second Mega-Arbitration Award).

<sup>7</sup> *Complaint and Request for Expedited Ruling of Time Warner Communications*, Docket No. 18082, (Mar. 2, 1998).

<sup>8</sup> *Southwestern Bell Telephone Company v. Public Utility Commission of Texas*, No. MO-98-CA-43, 1998 U.S. Dist. LEXIS 12938 (W.D. Tex., Jun. 16, 1998).

<sup>9</sup> *SWBT v. Public Utility Commission, et. al.*, No. 98-50787, 208 F.3d 475; 2000 U.S. App. LEXIS 5642 (5<sup>th</sup> Cir., 2000).

agreed with their dispositions of it, stating that “[t]he conclusion that modem calls terminate locally for purposes of compensation is both well-reasoned and supported by substantial evidence.”<sup>10</sup>

### **The Reciprocal Compensation Requirement Of Section 251(b)(5)**

Under section 251(b)(5), each local exchange carrier has the duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications. The FCC has construed this provision to apply only to the provision of “local telecommunications traffic”. Before the Court of Appeals, incumbent LECs argued that section 251(b)(5) preempts state commission authority to compel payments to CLECs; however, the Court of Appeals did not rule on that portion of the case.

We do not agree that section 251(b)(5) preempts state authority in establishing reciprocal compensation policy and rates. While section 251(d) gives the Commission authority to establish regulations to implement the requirements of section 251, it also states that the Commission shall not preclude any regulation, order, or policy of a State commission that: establishes access and interconnection obligations of local exchange carriers; is consistent with the requirements of the section; and does not substantially prevent implementation of the requirements of the section. There is no need for preemption of the state regulatory role in this regard. Many state regulatory agencies, including the PUCT, have expended thousands of hours

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<sup>10</sup> *Id.*, Section II.

of scarce staff resources in order to pursue the implementation of the competitive provisions of the Telecommunications Act.

Even in the event that the Commission affirms its earlier determination that ISP-bound traffic is not jurisdictionally local, then the PUCT urges the Commission to continue allowing state regulators to oversee the successful process of negotiation and arbitration under sections 251 and 252 of the Act.

In order to provide a more consistent framework for the application of reciprocal compensation for ISP-bound traffic, the PUCT welcomes the opportunity to provide added input into the development of additional FCC rules that would establish nationwide guidelines for this interconnection issue.

### **New Inter-Carrier Compensation Arrangements For ISP-Bound Traffic**

The PUCT has just completed an evidentiary proceeding to re-examine and establish rates and conditions for ISP-bound traffic.<sup>11</sup> This proceeding consolidated the issue of reciprocal compensation from several pending arbitration cases. After extensive hearings and conferences, with participation by many industry parties,<sup>12</sup> the PUCT determined that symmetric rates, based on SWBT's costs, should apply. The PUCT adopted a bifurcated rate structure (consisting of a

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<sup>11</sup> *Proceeding to Examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecommunications Act of 1996*, Docket No. 21982.

<sup>12</sup> Parties in this proceeding include: Adelphia Business Solutions of Texas, LLP, Allegiance Telecom of Texas, Inc., AT&T Communications of the Southwest, Inc., CCTX, Inc. D/B/A Connect!, e.spire Communications, Inc., Focal Communications Corp., Level 3 Communications, MCI Worldcom Communications, Inc., Southwestern Bell Telephone Company, Taylor Communications Group, Inc., and a coalition of CLECs that include Time Warner Telecom, L.P., KMC Telecom, Inc., GST Telecom, Inc., NEXTLINK Texas, Inc., Intermedia Communications, Inc.,

per call and per minute element) for end-office switching. The PUCT determined that two rate formulas for tandem switching and end-office transport may be applied, depending on the CLEC's tandem functionality. The PUCT's Order in this proceeding is attached.

Even though the PUCT has been called upon to arbitrate numerous inter-carrier interconnection disputes, including the issues related to reciprocal compensation, we support the FCC's position that commercial negotiations, driven by market forces, are the optimal means for establishing interconnection agreements.

### **The Transport Rule**

The PUCT raises one additional issue that was discussed in our recent proceeding, regarding the application of symmetrical tandem rates. The Commission's discussion in the First Report and Order<sup>13</sup> includes the possibility that "additional costs" incurred when transporting and terminating a call from another LEC may vary depending on whether tandem switching is involved. The Order anticipates that states may establish rates based on a number of factors, including the application of new technologies that may perform functions similar to that of a tandem switch in the provision of service. However, the FCC's rule 47 CFR 51.711 is not clear that states may consider new technologies in the establishment of relevant rates, and under one reading, compels a state commission to include the tandem rate once a showing of geographic coverage has been made. This lack of clarity resulted in a great deal of debate during the hearing

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IGC Choicecom, L.P., Telegent, Inc., Winstar Wireless of Texas, Inc., and Reliant Energy.

<sup>13</sup> *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, *Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket No. 95-185, First Report and Order, FCC 96-235, ¶ 1090 (Aug. 8, 1996).

on the merits in our recent proceeding, and we respectfully request that the Commission reconsider and possibly repeal this rule in the near future.

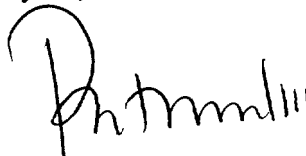
### **Conclusion**

The reciprocal compensation issue is one of many devilish details that has been identified and successfully addressed by state regulators. We encourage the Commission to continue its reliance upon and cooperation with state regulators in the implementation of the competitive aspects of the Telecommunications Act.

Respectfully submitted,


Public Utility Commission of Texas  
1701 N. Congress Ave.  
P.O. Box 13326  
Austin, Texas 78711-3326

July 12, 2000




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Pat Wood, III  
Chairman

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Judy Walsh  
Commissioner

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Brett A. Perlman  
Commissioner



DOCKET NO. 21982

PROCEEDING TO EXAMINE  
RECIPROCAL COMPENSATION  
PURSUANT TO SECTION 252 OF THE  
FEDERAL TELECOMMUNICATIONS  
ACT OF 1996

§ PUBLIC UTILITY COMMISSION  
§  
§ OF TEXAS  
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ARBITRATION AWARD  
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**DOCKET NO. 21982**

<b>PROCEEDING TO EXAMINE</b>	§	<b>PUBLIC UTILITY COMMISSION</b>
<b>RECIPROCAL COMPENSATION</b>	§	
<b>PURSUANT TO SECTION 252 OF THE</b>	§	<b>OF TEXAS</b>
<b>FEDERAL TELECOMMUNICATIONS</b>	§	
<b>ACT OF 1996</b>	§	

**ARBITRATION AWARD**

This Arbitration Award (Award) approves permanent rates for inter-carrier compensation relating to the transport and termination of local traffic between Southwestern Bell Telephone Company (SWBT) and certain competitive local exchange carriers (CLECs). Specifically, these rates provide reciprocal compensation for the inter-office transport, end-office switching, and tandem switching of local traffic. For purposes of this Award, a call to an Internet service provider (ISP) is subject to these reciprocal compensation rates to the extent that such a call originates and terminates within the same local calling area.

SWBT and any CLEC that has requested arbitration of the issue of inter-carrier compensation in this proceeding<sup>1</sup> pursuant to § 252 of the federal Telecommunications Act of 1996<sup>2</sup> shall incorporate the rates approved in this Award in any interconnection agreement which is subject to the outcome of this proceeding. If the CLEC has formally notified the Commission of its election of either the first or third option regarding reciprocal compensation for local traffic in Attachment 12 of the Texas 271 Agreement (T2A)<sup>3</sup>, then a true-up of the applicable bill-and-keep period shall be performed using the inter-carrier rates approved in this Award.<sup>4</sup>

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<sup>1</sup> Order No. 3 required CLECs to file petitions seeking arbitration of the issue of inter-carrier compensation in this proceeding by February 3, 2000. Order No. 3 at 1 (Jan. 25, 2000).

<sup>2</sup> Pub. L. No. 104-104, 110 Stat. 56 (codified as amended in scattered sections of 15 and 47 U.S.C.) (FTA).

<sup>3</sup> *Investigation of Southwestern Bell Telephone Company's Entry into the Texas InterLATA Telecommunications Market*, Project No. 16251, Order No. 55 (Oct. 13, 1999). The T2A is a standardized interconnection agreement available from SWBT through October 13, 2003. See Project No. 16251, Order No. 55, Attachment 12 at ¶ 4.1; Docket No. 16251, SWBT Letter Agreeing to Extend T2A (July 7, 2000). Attachment 12 to the T2A addresses the issue of reciprocal compensation, providing an electing CLEC with three options from which to choose. Under the first option, after January 22, 2000, SWBT and the electing CLEC shall operate under a bill-and-keep arrangement for all wireline traffic, including ISP-bound traffic, during periods of negotiation and/or

## I. JURISDICTION

If an incumbent local exchange carrier (ILEC) and CLEC cannot successfully negotiate rates, terms and conditions in an interconnection agreement, FTA § 252(b)(1) provides that either of the negotiating parties "may petition a State commission to arbitrate any open issues." The Commission is a state regulatory body responsible for arbitrating interconnection agreements approved pursuant to the FTA.

## II. PROCEDURAL HISTORY

On January 13, 2000, the Commission initiated this proceeding for the purpose of consolidating requests to arbitrate the issue of reciprocal compensation for the transport and termination of local traffic. This proceeding addresses only this single issue; other issues for which arbitration is requested by the carriers participating in this docket are addressed in separate arbitration proceedings relating to specific interconnection agreements. The Commission limited participation in this docket to only those parties arbitrating the issue of reciprocal compensation in this proceeding, *i.e.*, SWBT and interconnecting CLECs,<sup>5</sup> consistent with P.U.C. SUBST. R. 22.305(e).<sup>6</sup>

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arbitration. The second option permits the parties to operate under a bill-and-keep arrangement for the duration of their agreement. Under the third option, commencing on the date that the CLEC opts into the T2A, SWBT and the electing CLEC seeking to negotiate and/or arbitrate the issue of compensation shall operate under a bill-and-keep arrangement for all wireline traffic, including ISP-bound traffic, during periods of negotiation and/or arbitration. The bill-and-keep arrangements under both the first and third options are subject to true-up. The Commission concludes that the true-up period under the first and third options ends upon the Commission's approval of an interconnection agreement incorporating the inter-carrier compensation rates approved in this Award.

<sup>4</sup> After a CLEC files notification of its intent to opt into the T2A, in whole or in part, the Commission issues a letter of acknowledgement.

<sup>5</sup> See generally Order No. 3 (Jan. 25, 2000). GTE Southwest, Inc. and other ILECs did not seek to expand the scope of this proceeding to arbitrate reciprocal compensation issues for purposes of their interconnection agreements.

<sup>6</sup> This rule allows only the parties to the interconnection agreement to participate as parties in the arbitration proceeding.

The parties in this proceeding are: Adelphia Business Solutions of Texas, LLP (Adelphia), Allegiance Telecom of Texas, Inc. (Allegiance), AT&T Communications of the Southwest, Inc. (AT&T), CCTX, Inc. D/B/A Connect! (Connect), the CLEC Coalition<sup>7</sup> (the Coalition), e.spire Communications, Inc. (e.spire), Focal Communications Corp. (Focal), Level 3 Communications (Level 3), MCI Worldcom Communications, Inc. (WCOM), Southwestern Bell Telephone Company (SWBT), and Taylor Communications Group, Inc. (Taylor Comm.).<sup>8</sup>

The parties engaged in discovery through April 4, 2000. Direct testimony was filed on March 15, 17, and 20, 2000; rebuttal testimony was filed on March 31, 2000. The hearing on the merits was held on April 4 and 5, and May 18, 2000.

### III. RELEVANT STATE AND FEDERAL PROCEEDINGS

#### A. RELEVANT COMMISSION DECISIONS

##### *Mega-Arbitrations*

The FTA became effective in February 1996. Soon thereafter, several proceedings—collectively referred to as the Mega-Arbitrations—were initiated and consolidated for the purpose of arbitrating the first interconnection agreements in Texas under the new federal statute. A focal issue in these proceedings revolved around establishing “reciprocal compensation” rates. “Reciprocal compensation” refers to the statutorily mandated arrangement between two carriers

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<sup>7</sup> The CLEC Coalition includes: Time Warner Telecom, L.P. (TW), KMC Telecom, Inc. (KMC), GST Telecom, Inc. (GST), NEXTLINK Texas, Inc. (NEXTLINK), Intermedia Communications, Inc. (Intermedia), ICG Choicecom, L.P. (ICG), Teligent, Inc. (Teligent), Winstar Wireless of Texas, Inc. (Winstar), and Reliant Energy (Reliant).

<sup>8</sup> With the exception of WCOM and Taylor Comm., the CLECs participating in this docket filed requests to arbitrate the reciprocal compensation issue in this proceeding. WCOM and Taylor became parties to this proceeding by virtue of the severance of the issue of reciprocal compensation from other arbitration proceedings and the consolidation of such severed issue into this proceeding. *Petition of Southwestern Bell Telephone Company for Arbitration with MCI Worldcom Communications, Inc., Pursuant to Section 252(b)(1) of the Federal Telecommunications Act of 1996*, Docket No. 21791, Order No. 6 (Jan. 26, 2000); *Petition of Taylor Communications Group, Inc. for Arbitration with Southwestern Bell Telephone Company Pursuant to Section 252(b)(1) of the Federal Telecommunications Act of 1996*, Docket No. 21754, Order No. 7 (Jan. 24, 2000).

by which each carrier receives compensation for the transport and termination on its network facilities of local telecommunications traffic that originates on the network facilities of the other carrier.<sup>9</sup>

In November 1996, the Commission issued the First Mega-Arbitration Award in Docket No. 16189,<sup>10</sup> which established inter-carrier compensation rates, on an interim basis, for end-office switching, tandem switching, and inter-office transport. The reciprocal compensation rates adopted in the First Mega-Arbitration Award applied to calls that originated and terminated within SWBT's mandatory single- or multi-exchange local calling areas, including areas encompassed by mandatory Extended Area Service (EAS) arrangements. During the first nine months after the date upon which the first commercial call terminated between SWBT and a CLEC, however, the Commission designated "bill-and-keep"<sup>11</sup> as the arrangement by which reciprocal compensation would be accomplished.

The Second Mega-Arbitration Award in Docket No. 16189,<sup>12</sup> issued December 1997, approved cost studies for SWBT and established permanent inter-carrier compensation rates. These permanent rates appear in Attachment A to this Award.

Pursuant to FTA § 252(i), many CLECs subsequently opted into the reciprocal compensation provisions in the interconnection agreements approved in the Mega-Arbitration proceedings. Neither the First nor Second Mega-Arbitration Award, or the interconnection

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<sup>9</sup> See FTA §§ 251(b)(5), 252(d)(2). The FCC has construed the reciprocal compensation requirement in the FTA to apply to *local* telecommunications traffic only. 47 C.F.R. § 51.701(e) (1998).

<sup>10</sup> *Petition of MFS Communications Company, Inc. for Arbitration of Pricing of Unbundled Loops Agreement Between MFS Communications Company, Inc. and Southwestern Bell Telephone Company*, Docket No. 16189, *et al*, Award (Nov. 8, 1996) (First Mega-Arbitration Award).

<sup>11</sup> FTA § 252(d)(2)(B)(i) permits "arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements)."

<sup>12</sup> *Petition of MFS Communications Company, Inc. for Arbitration of Pricing of Unbundled Loops Agreement Between MFS Communications Company, Inc. and Southwestern Bell Telephone Company*, Docket No. 16189, *et al*, Award (Dec. 19, 1997) (Second Mega-Arbitration Award).

agreements resulting from those proceedings, specifically addressed the issue of whether an ISP-bound call is subject to reciprocal compensation.

*Docket No. 18082*

The reciprocal compensation provisions in the interconnection agreements approved in the Mega-Arbitration proceedings were initially disputed in Docket No. 18082.<sup>13</sup> In October 1997, Time Warner Communications of Austin L.P., Time Warner Communications of Houston, L.P., and FIBRcom (collectively, TW Comm) filed a complaint pursuant to Subchapter Q of the Commission's procedural rules, alleging that SWBT had breached its interconnection agreement with TW Comm. Specifically, the controversy centered on compensation for calls connecting SWBT customers to TW Comm customers that are ISPs. SWBT had refused to compensate TW Comm for such calls according to the reciprocal compensation rates in the interconnection agreement, based on its contention that those calls were not "local" in nature.

The Commission rejected SWBT's position and concluded that the calls in controversy were subject to the interconnection agreement's provisions relating to reciprocal compensation for the transport and termination of local traffic. In reaching this conclusion, the Commission first examined the nature of an ISP-bound call. It found that a call over the Internet consists of two components: (1) the information service component, which is the content of the call, and (2) the telecommunications service component, which is the carrier-to-carrier and carrier-to-end-user transmission of the call. With respect to the latter, the Commission concluded that when a person calls an ISP within a local calling area, the traffic carried on the call's transmission path is local in nature, with the telecommunications service component of the call terminating at the ISP.<sup>14</sup>

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<sup>13</sup> *Complaint and Request for Expedited Ruling of Time Warner Communications*, Docket No. 18082, Order (Feb. 27, 1998).

<sup>14</sup> In finding that such traffic is local in nature, the Commission rejected SWBT's end-to-end analysis of an ISP-bound call, which viewed the call as terminating at the website or websites ultimately accessed by the calling party, rather than at the ISP.

Having reached this conclusion, the Commission then found that the scope of the definition of "local traffic" in the interconnection agreement included ISP traffic. The interconnection agreement's definition stated that, for reciprocal compensation purposes, "local traffic" includes (1) a call that originates and terminates in the same SWBT exchange area, or (2) originates and terminates within different SWBT exchanges that share a common mandatory calling area, *e.g.*, mandatory EAS, mandatory extended local calling service (ELCS), or any other service with a mandatory expanded local calling scope. The definition did not distinguish types of calls (*i.e.*, Internet versus voice), but rather focused upon the area in which the call originated and terminated. Therefore, if a call to an ISP originated and terminated within the same exchange or mandatory calling area, the traffic terminating at the ISP constituted "local traffic" and, consequently, was subject to the reciprocal compensation rates for such traffic, as specified in the interconnection agreement.

*Other Post-Interconnection Agreement Disputes*—Other post-interconnection agreement disputes between ILECs, including SWBT, and CLECs involving the same issue arose after the Commission's ruling in Docket No. 18082. In those subsequent proceedings interpreting specific interconnection agreements, the Commission applied the precedent established in Docket No. 18082 in finding that the transport and termination of calls to ISPs is subject to reciprocal compensation.<sup>15</sup>

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<sup>15</sup> See *Petition of Waller Creek Communications, Inc. for Arbitration with Southwestern Bell Telephone Company*, Docket No. 17922, Order Approving Interconnection Agreement (April 28, 1998); *Complaint of Taylor Communications Group, Inc. Against Southwestern Bell Telephone Company*, Docket No. 18975, Order No. 3 (May 4, 1998); *Complaint and Request for Expedited Ruling of Golden Harbor of Texas, Inc.*, Docket No. 19160, Arbitrator's Decision (June 30, 1998); *Petition for Arbitration Pursuant to FTA § 252(b) to Establish Interconnection Agreement with GTE Southwest Incorporated*, Docket No. 20028, Arbitration Award (Feb. 22, 1999); *Complaint of MFS Against GTE Southwest, Inc. Regarding GTE's Nonpayment of Reciprocal Compensation*, Docket No. 21706, Preliminary Order (April 13, 2000).

**B. RELEVANT FEDERAL COMMUNICATIONS COMMISSION DECISIONS***Declaratory Order and Notice of Proposed Rulemaking*

The issue of whether ISP traffic is subject to reciprocal compensation also arose in other states. In response to formal and informal requests to clarify whether a carrier is entitled to receive reciprocal compensation for traffic delivered to an ISP, the Federal Communications Commission (FCC) issued a declaratory ruling and notice of proposed rulemaking in early 1999.<sup>16</sup>

The FCC's declaratory ruling concluded that ISP-bound traffic is jurisdictionally mixed and appears to be largely interstate in nature. In reaching this conclusion, the FCC rejected the notion that a call to an ISP is divisible into two separate parts, the information service component and the telecommunications service component. Rather, it focused upon the end-to-end nature of the communication, the approach traditionally used by the agency in determining whether a communication is intra- or interstate in nature. Finding that "[a]n Internet connection does not have a point of 'termination' in the traditional sense," the FCC found that a call to an ISP does not terminate at the ISP, but instead continues to its ultimate destination of an Internet website that is often located in another state or country. As a result of these conclusions, the FCC determined that FTA § 251(b)(5) does not *impose* any reciprocal compensation requirement for ISP-bound traffic.

Despite this statutory interpretation, however, the FCC stated that its conclusion did not, in and of itself, preclude the application of reciprocal compensation to the transport and termination of ISP-bound traffic. The FCC observed that parties to interconnection agreements may have agreed to the payment of reciprocal compensation for ISP-bound traffic, or that state commissions may have concluded that such compensation is due for such traffic in arbitration

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<sup>16</sup> *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, Declaratory Ruling; *Inter-Carrier Compensation of ISP-Bound Traffic*, CC Docket No. 99-68, Notice of Proposed Rulemaking, 14 FCC Rcd 3689 (Feb. 26, 1999).



and other proceedings conducted pursuant to FTA § 252. Until it addressed the matter of appropriate inter-carrier compensation for ISP-bound traffic further in a rulemaking proceeding, the FCC stated that interconnecting parties continued to be bound by their existing agreements, as interpreted by state commissions, with respect to the issue of reciprocal compensation in the context of ISP-bound traffic.

Finally, the FCC expressed its desire that carriers, in the first instance, establish inter-carrier compensation for ISP-bound traffic based on interconnection agreement negotiations. In view of the need to further develop the record for the purpose of adopting a rule regarding inter-carrier compensation for ISP-bound traffic, the FCC solicited comments on two alternative proposals to govern carriers' negotiations on this issue.<sup>17</sup>

### C. RELEVANT COURT DECISIONS

*Judicial Appeal of Docket No. 18082: Southwestern Bell Telephone Company v. Public Utility Commission of Texas (U.S. District Court; Western District, Texas; Midland/Odessa Division)*

SWBT appealed the Commission's order in Docket No. 18082 to federal district court, seeking declaratory and injunctive relief.<sup>18</sup> The federal district court affirmed the Commission's decision. After discussing the interstate characteristics of the Internet and the FCC's unique regulatory treatment of the Internet, the federal district court concurred in the Commission's two-component analysis of an ISP-bound call, and characterized the call terminating at the ISP as local traffic. The federal district court further concluded that the Commission relied upon substantial evidence to conclude that the SWBT/Time Warner interconnection agreement

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<sup>17</sup> The comments filed by the Commission in response to this notice of proposed rulemaking agreed with the FCC's position that commercial negotiations are the optimal means for establishing interconnection agreements. Furthermore, the Commission stated that the resolution of the reciprocal compensation issue is best determined under the aegis of the FCC and FTA §§ 251 and 252. *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98; *Inter-Carrier Compensation of ISP-Bound Traffic*, CC Docket No. 99-68, Comments of the Public Utility Commission of Texas (April 8, 1999).

<sup>18</sup> *Southwestern Bell Telephone Company v. Public Utility Commission of Texas*, No. MO-98-CA-43, 1998 U.S. Dist. LEXIS 12938 (W.D. Tex., June 16, 1998).

required the originating carrier to pay reciprocal compensation for calls to ISPs within the same local calling area.

*Judicial Appeal of Docket No. 18082: Southwestern Bell Telephone Company v. Public Utility Commission of Texas (U.S. Court of Appeals, Fifth Circuit)*

SWBT subsequently appealed the federal district court's decision to the Fifth Circuit court of appeals.<sup>19</sup> The court of appeals affirmed the lower court's decision. After denying SWBT's challenges to the Commission's exercise of jurisdiction in Docket No. 18082, the federal appellate court concluded that the Commission's decision in Docket No. 18082 did not conflict with the FTA, FCC rules, or FCC rulings. Citing language from the FCC's declaratory ruling on ISP-bound traffic, it found that a state commission may lawfully interpret an interconnection agreement as requiring reciprocal compensation for ISP-bound traffic, particularly given the FCC's past policy of treating ISP traffic as if it were local traffic in other contexts. Furthermore, the federal district court held that the Commission properly interpreted the SWBT/Time Warner interconnection agreement to impose reciprocal compensation obligations for calls to ISPs within a local calling area.<sup>20</sup>

*Judicial Appeal of FCC's Declaratory Order: Bell Atlantic Telephone Companies v. Federal Communications Commission (U.S. Court of Appeals, D.C. Circuit)*

Bell Atlantic and a group of CLECs appealed the FCC's declaratory ruling to the District of Columbia (D.C.) Circuit court of appeals.<sup>21</sup> The appellate court vacated the FCC's decision and remanded the proceeding to the federal agency for want of reasoned decision-making. The appellate court concluded that the FCC failed to adequately explain why an end-to-end analysis, which the federal agency has traditionally used to determine the jurisdictional nature of a

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<sup>19</sup> *Southwestern Bell Telephone Company v. Public Utility Commission of Texas*, 208 F.3d 475 (5<sup>th</sup> Cir. 2000).

<sup>20</sup> Throughout its opinion, the court of appeals cited extensively to another federal appellate court's decision on the same issues in support of its conclusions. See *Illinois Bell Telephone Company v. Worldcom Techs., Inc.*, 1790 F.3d 566 (7<sup>th</sup> Cir. 1999).

<sup>21</sup> *Bell Atlantic Telephone Companies v. Federal Communications Commission*, 206 F.3d 1 (D.C. Cir. 2000).

*previously concluded that ISP-bound traffic is local in nature and reaffirms that such traffic is eligible for reciprocal compensation in this proceeding. Its prior rulings remain viable from technological, policy, and legal standpoints, and they are now supported by the federal appellate court decisions in Southwestern Bell Telephone Co. v. Public Utility Commission of Texas and Bell Atlantic Telephone Companies v. Federal Communications Commission. Moreover, designating ISP-bound traffic as local traffic is not inconsistent with any action taken by the FCC on the matter. Even if the designation of ISP-bound traffic as local is subject to future challenge at the FCC and/or in the courts, the Commission finds independently that it is reasonable to compensate such traffic as local traffic. Finally, the Commission concludes that there are no compelling policy reasons for establishing a reciprocal compensation mechanism that would require the separation and/or measurement of ISP-bound traffic.*

*The Commission also reaffirms its previous determination that reciprocal compensation arrangements apply to calls that originate from and terminate to an end-user within a mandatory single or multi-exchange local calling area, including the mandatory EAS/ELCS areas comprised of SWBT exchanges and the mandatory EAS/ELCS areas comprised of SWBT exchanges and exchanges of independent ILECs.<sup>54</sup> The Commission finds that to the extent that FX-type and 8YY traffic do not terminate within a mandatory local calling scope, they are not eligible for reciprocal compensation. The Commission reiterates that this Award does not preclude CLECs from establishing their own local calling areas or prices for purpose of retail telephone service offerings.<sup>55</sup>*

*Finally, the Commission agrees with SWBT that transit traffic should not be eligible for reciprocal compensation. The Commission addresses transit traffic in its discussion of DPL Issue No. 4.*

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<sup>54</sup> See First Mega-Arbitration Award at ¶58; Project No. 16251, Order No. 55, Attachment 12 at ¶ 1.1. See also Evaluation of the Public Utility Commission of Texas, *In the Matter of Application of SBC Communications Inc., and Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. D/B/A/ Southwestern Bell Long Distance for Provision of In-Region, InterLATA Services in Texas Pursuant to Section 271 of the Telecommunications Act of 1996 To Provide In- Region*, CC Docket No. 00-4, at 88 (Jan. 31, 2000); Project No. 16251, Final Staff Report on Collaborative Process at 103-104 (Nov. 18, 1998).

<sup>55</sup> See First Mega-Arbitration Award at ¶59.

the one exception to its proposal is AT&T's Feature Group D access traffic, which is generated via its long-distance network.<sup>48</sup> Furthermore, AT&T agrees with the Coalition that ISP-bound traffic is local traffic, possessing all the cost and technical characteristics of a local call.<sup>49</sup> AT&T argues that a CLEC should be compensated for any costs that it incurs in terminating a call from a SWBT customer because SWBT avoids having to incur those costs.<sup>50</sup>

With regards to 8YY traffic, AT&T asserts that an 8YY call that originates on one carrier's network and terminates on another's network without the need for any interexchange carrier (IXC) transport is carried on local interconnection trunks and, therefore, is subject to reciprocal compensation.<sup>51</sup> AT&T further argues that virtual FX traffic and Internet Gateway traffic should not be treated differently from other local traffic. It states that there are no underlying routing or geographic characteristics that uniquely distinguish such traffic from other types of local calls. AT&T observes that, depending upon the physical boundaries of a customer's pre-defined local calling area, a local call may well traverse more central offices and route miles than a given toll call.<sup>52</sup> Moreover, AT&T contends that SWBT's position regarding Internet Gateway traffic would discriminate based on a CLEC's technology and network architecture and would be anti-competitive.<sup>53</sup>

**(c) Commission Decision**

*The Commission is again not persuaded by SWBT's argument that it should treat ISP-bound traffic differently for purposes of reciprocal compensation. The Commission has*

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<sup>47</sup> AT&T Initial Post-Hearing Brief at 5 (April 19, 2000).

<sup>48</sup> AT&T Ex. No. 5, Direct Testimony of Maureen A. Swift at 12.

<sup>49</sup> AT&T Initial Post-Hearing Brief at 11 (April 19, 2000).

<sup>50</sup> *Id.* at 12.

<sup>51</sup> AT&T Ex. No. 5, Direct Testimony of Maureen A. Swift at Direct at 12.

<sup>52</sup> AT&T Ex. No. 4, Rebuttal Testimony of Patricia D. Kravtin at 20.

<sup>53</sup> *Id.*

telephone network in identical ways.<sup>42</sup> Furthermore, the Coalition contends that there is no cost basis for any such differentiation because the cost driver for both types of calls is the same.<sup>43</sup>

The Coalition also asserts that the Commission should reject SWBT's effort to parse out different forms of terminating arrangements for serving ISPs by exempting certain arrangements such as "virtual FX" and "Internet Gateways" from reciprocal compensation. First, the Coalition argues that SWBT's effort to carve out such exemptions is unfounded, both as a matter of technology and as a matter of economic policy.<sup>44</sup> With respect to the so-called Internet Gateway issue, the Coalition contends that the Commission's determination of when reciprocal compensation is due should be technology-neutral. The Coalition believes given the rapid development of new technologies and the consumer demand for Internet access, the Commission should not take any action that would have the effect of dictating how a carrier deploys new technology or designs its networks to serve its customers.<sup>45</sup>

Second, with respect to the so-called virtual FX issue, the Coalition contends that the CLEC service described by SWBT is also provided by SWBT in essentially the same manner. The Coalition believes that any exemption afforded a CLEC's virtual FX traffic would result in discrimination against CLECs and provide a competitive advantage to SWBT's own similar offerings.<sup>46</sup>

AT&T avers that the most efficient and effective approach to addressing the reciprocal compensation issue is to adopt a cost-based rate structure covering all traffic exchanged between AT&T and SWBT which originates and terminates within the same LATA.<sup>47</sup> AT&T states that

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<sup>42</sup> Coalition Ex. No. ICG-3, Direct Testimony of Don J. Wood at 7.

<sup>43</sup> Coalition Ex. No. ICG-3, Direct Testimony of Don J. Wood at 7; Coalition's Initial Brief at 15-16 (April 19, 2000).

<sup>44</sup> Coalition Ex. No. CLEC-1, Direct Testimony of William Page Montgomery at 23-24.

<sup>45</sup> Allegiance Ex. No. 1, Direct Testimony of Richard Anderson at 2.

<sup>46</sup> Coalition Ex. No. CLEC-2, Rebuttal Testimony of William Page Montgomery at 37-39.

for the retail FX arrangement, the call would be an interexchange, intraLATA long-distance call.<sup>36</sup>

- 8YY traffic, which is traffic consisting of those calls which use “800”, “877”, or “888” as the area code.<sup>37</sup> SWBT posits that such calls are generally not subject to reciprocal compensation requirements and may be considered “local” for reciprocal compensation purposes only if the call originates and terminates in the same SWBT exchange area or within exchanges that share a common mandatory calling area.<sup>38</sup>

**(b) CLECs' Position**

The Coalition argues that all traffic originated by the customer of a carrier that is delivered by a terminating carrier pursuant to the calling party's request should be subject to reciprocal compensation.<sup>39</sup> The Coalition asserts that the Commission should re-affirm its precedent treating calls to ISPs as local calls subject to reciprocal compensation in accordance with FTA § 251(b)(5). In view of the D.C. Circuit court of appeals' criticism of the FCC's use of an end-to-end analysis to conclude that ISP-bound traffic is interstate in nature,<sup>40</sup> the Coalition posits that it is unlikely that the FCC, on remand, will develop a convincing analogy between ISP-bound traffic and long-distance traffic on remand to justify its declaratory ruling.<sup>41</sup> Even absent the federal appellate court's remand, the Coalition argues that the segregation of ISP traffic for reciprocal compensation purposes is not justified by any cost differences between ISP-bound traffic and other local traffic, given that the two types of calls use the public switched

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<sup>36</sup> SWBT Ex. No. 7, Direct Testimony of D. Randy Long at 10.

<sup>37</sup> The originating party using one of these area codes is not charged for the call. The carrier terminating the call typically pays for 8YY calls.

<sup>38</sup> SWBT Ex. No. 8, Rebuttal Testimony of D. Randy Long at 22.

<sup>39</sup> Coalition Ex. No. ICG-3, Direct Testimony of Don J. Wood at 7.

<sup>40</sup> *Bell Atlantic Telephone Companies v. Federal Communications Commission*, 206 F.3<sup>rd</sup> 1 (D.C. Cir. 2000).

<sup>41</sup> Coalition Ex. No. ICG-4, Rebuttal Testimony of Don J. Wood at 4-10.

call placed to an ISP has end-to-end connectivity to almost anywhere in the world--in other words, such a call is not terminated locally but rather to some point on the World Wide Web.<sup>30</sup> In support of this argument, SWBT relies upon the FCC's declaratory ruling addressing the nature of ISP-bound traffic as it relates to reciprocal compensation.<sup>31</sup>

SWBT also states that all local traffic originated through unbundled network elements (UNEs) is eligible for reciprocal compensation. SWBT explains that the manner in which a CLEC decides to originate its customers' calls is irrelevant as to whether reciprocal compensation applies to those calls, given that the CLEC's method of doing business does not affect SWBT's cost to terminate the traffic.<sup>32</sup> SWBT contends, however, that the following types of traffic are not eligible for reciprocal compensation:

- Traffic terminated through Internet Gateways, which generally are not used to originate traffic, but rather serve to receive traffic for purposes of routing that traffic to an ISP local server: SWBT contends that this type of traffic is not "local" in nature and that the traffic flow is inherently "one-way," *i.e.*, there is no exchange of originating and terminating traffic between the carriers.<sup>33</sup>
- Transit carriers: SWBT asserts that such a carrier (*i.e.*, the second or intermediate carrier) neither originates nor terminates the call, but simply directs the call to its destination, and is only entitled to recover the cost for transiting the call across its network.<sup>34</sup>
- FX-type traffic, which is traffic that originates in one local exchange area and is delivered to a telephone number that is assigned to that same local exchange area, although the physical premises for that telephone number and the customer are located in another local exchange area<sup>35</sup>: SWBT states that, but

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<sup>30</sup> SWBT Ex. No. 5, Direct Testimony of Robert Jayroe at 5.

<sup>31</sup> *In the Matter of the Implementation of Local Competition Provisions in the Telecommunications Act of 1996, Inter-Carrier Compensation for ISP-Bound Traffic*, CC Docket No. 96-98, Declaratory Ruling; *Inter-Carrier Compensation of ISP-Bound Traffic*, CC Docket No. 99-68 Notice of Proposed Rulemaking (Feb. 25, 1999).

<sup>32</sup> SWBT Ex. No. 8, Rebuttal Testimony of D. Randy Long at 21.

<sup>33</sup> SWBT Ex. No. 7, Direct Testimony of D. Randy Long at 7-9.

<sup>34</sup> SWBT Ex. No. 7, Direct Testimony of D. Randy Long at 12.

<sup>35</sup> SWBT Ex. No. 7, Direct Testimony of D. Randy Long at 10.

Calls originated by [CLEC's] end users and terminated to SWBT's end users (or vice versa) will be classified as "Local Traffic" under this Agreement and subject to reciprocal compensation if the call: (i) originates and terminates in the same SWBT exchange area; or (ii) originates and terminates within different SWBT exchanges, or within a SWBT exchange and an independent ILEC exchange, that share a common mandatory local calling area, *e.g.*, mandatory extended area service (EAS), mandatory extended local calling service (ELCS), or other types of mandatory expanded local calling scopes. For the purposes of reciprocal compensation, a call to an Internet Service Provider is classified as "Local Traffic" if it meets either requirement in (i) or (ii).

## V. DISCUSSION OF DPL ISSUES

This proceeding address the four issues in Joint Decision Point List (DPL) filed by the parties on February 22, 2000:

DPL Issue No. 1: What traffic should be subject to reciprocal compensation?

DPL Issue No. 2: What method should be used to determine inter-carrier compensation?

DPL Issue No. 3: What is the appropriate rate or rates (*e.g.*, symmetrical/asymmetrical) at which compensation should be made?

DPL Issue No. 4: What is the appropriate method by which to bill for this traffic?

### A. DPL ISSUE NO. 1: WHAT TRAFFIC SHOULD BE SUBJECT TO RECIPROCAL COMPENSATION?

#### (a) *SWBT's Position*

SWBT asserts that the FCC has determined that the FTA's reciprocal compensation requirement applies to the exchange of local traffic only. It defines "local traffic" as traffic that is either within a single exchange or traffic that is between exchanges subject to mandatory local calling; in either instance, such traffic falls within the "basic/local" retail calling scope of an exchange customer.<sup>29</sup> SWBT contends that ISP-bound traffic, however, does not originate and terminate within any such calling scope and is largely interexchange in nature. Consequently, SWBT avers that ISP-bound traffic is not subject to reciprocal compensation. It argues that a

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<sup>29</sup> SWBT Ex. No. 7, Direct Testimony of D. Randy Long at 6.



ISP-bound traffic; the scope of the reciprocal compensation requirement in FTA § 251(b)(5); and the relevance of terms such as “termination”, “telephone exchange service”, “exchange access service”, and “information access” to the issue of reciprocal compensation in the context of ISP-bound traffic. Furthermore, the notice requested comment on any new or innovative inter-carrier compensation arrangements for ISP-bound traffic that are currently under consideration or that have been adopted through negotiation or arbitration.

#### IV. INTER-CARRIER COMPENSATION RATES

The inter-carrier compensation rates approved in the Mega-Arbitrations, as reflected in Attachment A to this Award, form the basis of the inter-carrier compensation rates approved in this Award pursuant to FTA § 252(d)(2). The inter-office transport and tandem switching rates approved in the Mega-Arbitration proceedings are re-adopted in this Award. For the calculation of the bifurcated end-office switching rate approved in this docket, the Commission relies upon the local switching cost studies approved in the Mega-Arbitrations and the Basic Network Function (BNF) cost studies approved in Project No. 16657.<sup>26</sup> For purposes of the methodology approved in this Award for calculating a blended tandem switching rate, the tandem switching and inter-office transport rates approved in the Mega-Arbitrations are elements in the methodology, as well as the bifurcated end-office switching rate approved in this Award.

Consistent with the First Mega-Arbitration Award,<sup>27</sup> the T2A<sup>28</sup>, and Section V.A. of this Award, the following definition of “Local Traffic” will apply to the inter-carrier rates approved in this Award and shall be incorporated in affected interconnection agreements:

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<sup>25</sup> *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98; and *Inter-Carrier Compensation of ISP-Bound Traffic*, CC Docket No. 99-68, Public Notice (June 23, 2000).

<sup>26</sup> *Southwestern Bell Telephone Company's Application for Approval of LRIC Studies for Basic Network Access Channel Nonstandard 4-Wire, Type O, et al., Pursuant to P.U.C. SUBST. R. 23.91*, Order No. 8 (Nov. 12, 1997).

<sup>27</sup> First Mega-Arbitration Award at ¶58 (Nov. 8, 1996).

<sup>28</sup> Docket No. 16251, Order No. 55, Attachment 12 at ¶ 1.1.

communication, made sense in the context of the reciprocal compensation issue, in terms of both the FTA and FCC rules. Specifically, it found that “[the FCC] has yet to provide an explanation why this inquiry is relevant to discerning whether a call to an ISP should fit within the local call model of two collaborating LECs or the long-distance model of a long-distance carrier collaborating with two LECs.”<sup>22</sup>

In remanding the matter to the FCC, the court of appeals made several observations about the fallacies in the FCC’s reliance on the end-to-end analysis in addressing the reciprocal compensation issue. The appellate court noted that a call to an ISP appears to fit within the definition of “termination” in the FCC’s rules, that is, the traffic is switched by the carrier whose customer is the ISP and then delivered to the ISP.<sup>23</sup> The FCC, however, failed to apply or mention this definition in its declaratory ruling, instead relying on an end-to-end analysis previously applied in contexts that the appellate court characterized as different and distinct from the context of Internet communications. The appellate court also criticized the contradiction in the FCC’s application of the end-to-end analysis to characterize ISP-bound traffic as interstate traffic in view of the FCC’s prior rulings exempting ISPs and other interactive computer services from access charges. Finally, the court of appeals pointed out the lack of satisfactory explanation offered by the FCC as to how its conclusions with regard to ISP-bound traffic accord with the statutory definitions of “exchange access” and “telephone exchange service”.<sup>24</sup>

In June 2000, the FCC issued a notice seeking comments in response to the remand by the D.C. Circuit court of appeals.<sup>25</sup> The notice requested comment on the jurisdictional nature of

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<sup>22</sup> *Id.* In view of the grounds for remand, the court of appeals did not reach the issue raised by Bell Atlantic with respect to whether FTA § 251(b)(5) preempts state commissions from compelling reciprocal compensation payments for ISP-bound traffic.

<sup>23</sup> *Id.* The relevant FCC rule defines “termination” as “the switching of traffic that is subject to section 251(b)(5) at the terminating carrier’s end office switch (or equivalent facility) and delivery of that traffic from that switch to the called party’s premises” 47 C.F.R. 51.701(d).

<sup>24</sup> *See* 47 U.S.C. §§ 153(16), 153(47) (2000).